Report to the Responsible Minister for the Qulliq Energy Corporation On:

Qulliq Energy Corporation's 2010/11 General Rate Application, Phase II

Report 2012-01

January 27, 2012

THE UTILITY RATES REVIEW COUNCIL

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Julia Demcheson	Interpreter
Simeoni Natseck	Interpreter

QEC WITNESSES

The following attended one or more community consultations as representatives of Qulliq Energy Corporation:

Peter Mackey	President and CEO
Darryl Taylor	GRA Coordinator/Manager Regulatory Affairs

LIST OF ABBREVIATIONS

CEO	Chief Executive Officer
COS	Cost of Service
DSM	Demand Side Management
FERC	Federal Energy Regulatory Commission
FRSF	Fuel Rate Stabilization Fund
FSF	Fuel Stabilization Fund
FSR	Fuel Stabilization Rider
GN	Government of Nunavut
GRA	General Rate Application
KWh	Kilowatt Hour
NWTPUB	Northwest Territories Public Utilities Board
MWh	Megawatt Hour
O&M	Operation & Maintenance
NTPC	Northwest Territories Power Corporation
NUL-NWT	Northland Utilities Limited
QEC	Qulliq Energy Corporation
T&C	Terms and Conditions
URRC	Utility Rates Review Council
YEC	Yukon Energy Corporation

TABLE OF CONTENTS

EXECUTIVE SUMMARY

The Phase II Application filed by QEC on September 9, 2011, sets out, among others, the Corporation's proposed adjustments to base rates effective April 1, 2012. The Application includes the Corporation's cost of service study, a discussion of rate design principles, proposed rate schedules, proposed revisions to the Terms and Conditions of Service, proposed amendments to the Fuel Rate Stabilization Fund and responses to previous URRC directions and recommendations. The Application addresses rate rebalancing between communities and rate classes. The rate proposals in the Phase II Application are designed to recover the Corporation's 2010/11 revenue requirement approved by the Minister.

In its Application, QEC proposed that rates be established on the basis of a Nunavut wide cost of service study. QEC provided a number of reasons in support of the move to Nunavut wide rates. Adoption of Nunavut wide rates means moving away from the existing community based rates. This also means, rates in certain communities would have to increase while rates in other communities would decrease if target revenue to cost coverage ratios are to be met. QEC proposed that the rate changes needed to bring the revenue to cost coverage ratios to target levels, by community, be gradual and carried out over a number of years. For the proposed rates effective April 1, 2012, QEC proposed, the maximum increase for the domestic and commercial rate class in any community be limited to 5% and the maximum decrease limited to 4%.

Following public consultation meetings and full examination of the Application, the URRC recommends acceptance of QEC's proposal to adopt a Nunavut wide COS approach for the purpose of establishing rates. The URRC also considers as reasonable and appropriate, QEC's proposal to phase in, over a number of years, rate changes resulting from the transition to Nunavut wide COS approach and accepts QEC's proposal to limit the maximum increase for the domestic and commercial rate classes in any community to 5% and the maximum decrease to 4%, for rates effective April 1, 2012. The URRC recommends approval of the rates proposed by QEC effective April 1, 2012 and recommends approval of revisions to the Terms and Conditions of Service and amendments to the Fuel Rate Stabilization Fund, all as directed in this report.

1.0 BACKGROUND

The Qulliq Energy Corporation (QEC) filed a Phase I General Rate Application (GRA) for the 2010/11 test year with the responsible Minister for QEC on October 4, 2010. The responsible Minister referred the matter to the Utility Rates Review Council (URRC) for review and recommendations pursuant to Section 12 of the *Utility Rates Review Council Act* (the URRC Act).

The URRC completed its review of the Phase I GRA in March 2011 and issued Report 2011-01 dated March 2, 2011. Following his review of the report, the responsible Minister established and approved a 2010/11 test year revenue requirement of $101,198,000 for the Corporation. Base rate changes to recover the approved revenue requirement were implemented effective April 1, 2011. The rate increase approved by the responsible Minister was 18.88%.

By letter dated September 9, 2011, QEC filed Phase II of the General Rate Application (Application) for the 2010/11 test year. The responsible Minister, in turn, referred the matter to the URRC for review and recommendations, pursuant to Section 12 of the URRC Act.

The URRC Act requires the Corporation, as the supplier of electricity in Nunavut, to obtain the approval of the responsible Minister for any proposed rate changes. Before approving the Corporation's rates, the responsible Minister is required to seek the advice of the URRC.

In the case of Major applications, such as the current Phase II Application, the URRC is required to report to the responsible Minister within 150 days following receipt of a Request for Advice, its recommendation that:

a) the imposition of the proposed rate or tariff should be allowed;
b) the imposition of the proposed rate or tariff should not be allowed; or
c) another rate or tariff specified by URRC should be imposed.

With respect to Phase II applications, Section 1(3) of the URRC's Rate Setting Guidelines provide that:

- Rates for service provided by a utility shall not be unjustly discriminatory or unduly preferential. The Review Council should base its analysis of applications on this principle and report to Government accordingly;
- Rates for utility service should be designed to encourage the wise use of energy and the Review Council should report to Government in accordance with this principle.

In carrying out its purposes under the URRC Act, the URRC is permitted to:

a) hold public and private meetings;
b) retain the services of experts and advisors;
c) solicit advice from the public;
d) conduct meetings and mediations with utilities and concerned parties and assist utilities and their customers in developing a consensus on contentious issues;
e) require utilities and their employees to provide all information needed to carry out its purposes and may require that information be provided under oath or by way of solemn declaration; and
f) generally engage in activities that assist in providing informed advice to the responsible Minister.

Pursuant to the Request for Advice from the responsible Minister, dated September 9, 2011, the URRC conducted the proceedings in accordance with the requirements and parameters specified in the URRC Act. This report sets out the URRC's findings and recommendations to the responsible Minister.

2.0 APPLICATION

2.1 OVERVIEW OF APPLICATION

This is the first Phase II GRA application in the Corporation's history since division from the Northwest Territories Power Corporation (NTPC). The last cost of service (COS) study for Nunavut communities was conducted as part of NTPC's 1995/98 GRA. That application was prepared on the basis of a community-based approach to cost of service and rate design. The

previous GRA by the Corporation for the 2004/05 test year did not include an updated COS study. Rate adjustments since 2004/05 have generally been implemented on an equal percentage basis across all rate classes.

Following the URRC Report 2011-01 on the 2010/11 Phase 1 GRA, the responsible Minister established and approved a 2010/11 test year revenue requirement of $101,198,000 for the Corporation. An 18.88% increase in rates to recover the approved revenue requirement was implemented effective April 1, 2011 on an equal percentage basis across all rate classes and communities. The current Phase II Application is solely a rate rebalancing exercise between communities and rate classes to collect the revenue requirement approved by the minister in the Phase I GRA. Phase II does not seek to increase revenue; it determines how the approved 18.88% increase is to be collected from the various customer classes. A Phase II Application usually consists of two components, a cost of service study and a rate design proposal.

The Phase II Application sets out the Corporation's proposed adjustments to base rates effective April 1, 2012. The Application includes the Corporation's cost of service study, a discussion of rate design principles, proposed rate schedules, proposed revisions to the Terms and Conditions of Service, proposed amendments to the Fuel Rate Stabilization Fund, and responses to previous URRC directions and recommendations. The Application addresses rate rebalancing between communities and rate classes. Rate proposals in the Phase II Application are designed to recover the Corporation's approved 2010/11 revenue requirement.

In its Application, QEC proposes that rates be established on the basis of a Nunavut wide cost of service study. QEC provided a number of reasons in support of the move to Nunavut wide rates. Adoption of Nunavut wide rates means moving away from the existing community based rates. This also means rates in certain communities would have to increase while rates in other communities would have to decrease if target revenue to cost coverage ratios are to be met. QEC proposes that the rate changes needed to bring the revenue to cost coverage ratios to target levels, by community be gradual and carried out over a number of years. For the proposed rates effective April 1, 2012, QEC proposes the maximum increase for the domestic and commercial

rate class in any community be limited to 5% and the maximum decrease limited to 4%. QEC's Nunavut wide rate proposals are more fully discussed in the Sections that follow.

2.2 REQUESTED APPROVALS

In its Application letter dated September 9, 2011, QEC requested the following approvals:

> **"1. Approving the Corporation's proposed adjustments to base rates effective April 1, 2012:** Schedules 1.1.1-1.1.5 of the Application summarize the proposed adjustments to base rates. The proposed base rates were developed considering normal rate design criteria for Canadian Crown utilities and Government of Nunavut policy objectives. Details on the rate design criteria used to develop the rate proposals are set out in Chapter 7 of the Application.
>
> **2. Approving Fuel Rate Stabilization Fund adjustments:** The Corporation is proposing certain adjustments to the Fuel Rate Stabilization (FRS) Fund balance calculation and presentation. These proposed adjustments are discussed in Chapter 8 of the Application.
>
> **3. Approving the revised Terms and Conditions of Service:** The Corporation is proposing revisions to the Terms and Conditions of service as detailed in Chapter 9 of the Application.
>
> **4. For any such further and other instructions within the Minister's authority as the Corporation may request and the Minister determines proper."**

3.0 PROCESS FOR HEARING OF PHASE II OF THE GRA APPLICATION

Upon receipt of the Application, the URRC established a process for examination and hearing of the Application. Notice of the Application, followed by location and timing of community consultation meetings was published in newspapers having general circulation in Nunavut from September 23 to October 12, 2011 and from November 4 to 9, 2011. The URRC also notified Nunavut communities of the dates and locations of public consultation meetings through cable television advertisements, community bulletin boards and public announcements on CBC and local radio stations. The Mayors and Senior Administrative Officers in communities served by QEC as well as Members of the Legislative Assembly and Cabinet Ministers were notified of the Application and process, by letter.

As part of the process for examination of the Application, the URRC issued three sets of information requests to QEC. Responses to information requests were received on November 4, 2011, November 10, 2011 and December 2, 2011. Community consultation meetings were held in the following locations:

Places	**Dates**
Cape Dorset	Nov. 9 at 730PM
Iqaluit	Nov. 10 at 230PM and 630PM
Rankin Inlet	Nov. 12 at 230PM
Repulse Bay	Nov. 12 at 7PM
Taloyoak	Nov. 14 at 630PM
Cambridge Bay	Nov 15 at 230PM and 630PM

At the meetings, QEC presented a panel of witnesses headed by the CEO of the Corporation to explain the nature of the Phase II Application and the bill impacts on customers residing in different Nunavut communities. QEC made power point presentations explaining the alternatives considered and the reasons why QEC is proposing a move to Nunavut wide average rates. Meeting participants were provided an opportunity to make statements and ask questions of QEC's panel on the Phase II Application.

In accordance with the schedule established by the URRC, interested parties were given an opportunity to make written comments respecting the Application by December 16, 2011. Two written submissions were received indirectly at a later date. The URRC has considered the information contained in those submissions in forming this report.

4.0 COMMUNITY CONSULTATIONS

Cape Dorset:

One of the participants noted the expected addition of new plant in Cape Dorset and the corresponding impact on rates. QEC responded that the move to Nunavut wide rates proposed in the Phase II Application would minimize rate volatility in communities that require plant refurbishment, in comparison with the existing community based rates.

One participant noted the rate increase is a double hit. Not only will we pay for the electricity at our homes, but the stores will merely pass along their rate change in the cost of their goods. QEC acknowledged that commercial customers do have to pass along cost increases.

One participant thanked the URRC and indicated that the information tonight was not really as horrible as he thought it was going to be; in fact better than expected. He indicated that he didn't mind the recommendation at all.

On a general note, QEC indicated that it is intending to file more frequent rate applications in order to keep rate increases to more manageable levels.

Iqaluit:

One of the participants questioned QEC on how long it will take for the rate to become flat or the Nunavut wide rate to be fully achieved. In response QEC noted the shock that such a move would create if it tried to do it all at once. QEC stated it will take 2 – 3 GRAs to get there, and that is expected to take 9 – 10 years.

The same participant noted the Tourism sector is concerned that it will be adversely affected because not only will the rate go up for hotels, but for all businesses that rely on tourism. It may drive the attractiveness of the north as a tourist destination. QEC agreed, but noted each rate structure option goes the same way. It was noted that many communities' rates go down too, so overall it is hoped that the effect on Nunavut tourism will be minimized.

One participant representing homeowners noted that 17 plants across Nunavut require refurbishment. Why did QEC take so long before having a reasonable plan which might have moderated rate change?

In response QEC stated the Territory separation plans stopped all potential investment in infrastructure, including power plant needs. The matter was compounded by the rapid population growth which followed separation. QEC indicated it used the limited funds available to it just to keep existing plant running, not building new plants. QEC is trying to convince the Federal Government and Government of Nunavut (GN) to help offset costs so that not all of the rate increase effects land on the backs of ratepayers.

With regard to the plant refurbishment issue one participant noted that QEC spoke about this the last time QEC had a hearing. What has been the progress? In response QEC stated, right now the Federal Government has other financial issues that are of great concern, but QEC has presented its issues to them, especially the fact that the plants were not adequate at separation of the Territories, and feels that the Federal Government has listened, and that their requests are at least being considered; nothing concrete at this time. QEC noted that they are not seeking a handout; just that the Federal Government should have left the plants in better shape at the time of separation.

One participant questioned if QEC is not seeking more revenue, why is there an increase? QEC explained the Cost of Service process and the fact the Phase II Application is a zero sum game from an overall revenue perspective.

One participant questioned whether this is just a fait accompli; aren't the rates merely going up? In response QEC stated there will be an increase for Iqaluit regardless of what allocation method is recommended by the URRC and finally chosen by the GN. This Phase II process is to decide which option the URRC will recommend to GN.

Repulse Bay:

One resident expressed concern that QEC always estimates bills if they cannot get to the meter due to snow etc. He felt that this led to confusion and erroneous bills. He believed that the Company should get actuals all the time.

QEC indicated that often circumstances make it difficult to obtain meter reads, citing dogs and snow. However, QEC indicated that once an actual meter reading is obtained from an accessible meter, then all amounts are reconciled and corrected.

Another resident indicated his disagreement with QEC's process of estimating, citing that they are often in error by more than 50%. QEC responded by indicating that the process for making the estimates uses the amount consumed in the same month for the prior year and then using refinements based on the past few months of consumption. QEC considered this to be a good basis for estimates; in any event, QEC corrects all estimates when an actual read is obtained.

Taloyoak:

One participant questioned if hydro power were installed in Iqaluit and if a saving occurs, will it be shared? QEC responded in the affirmative and stated, the prefeasibility study shows there is a saving, especially once capital has been recovered. The participant indicated support for the same rate across Nunavut. If we did not do this, each community could face real hardship at some point. He noted that QEC has good operations in Taloyoak; he also sees the benefit of one rate.

An Elder of the community noted those on pensions always pay for power. Power subsidies for elders are needed. The pensions are low and it's all we have to pay for power – the bills are just too high. We cannot keep up to just the payments, let alone the increases. Elders should get larger discounts. In response QEC stated following Phase 1 of the GRA that Cabinet instructed all departments to work together to ensure that subsidies are fair. QEC indicated that comments reflecting the elder's views, if included in the Phase II decision, will help in those discussions so that all matters are properly considered for seniors.

The URRC Chair noted in the 2004/2005 proceeding, elders' concerns were fully reported to the Minister. Pensions are flat, and are the same all across Canada in spite of the very high cost of living in Nunavut.

One participant questioned where to go to see about a better subsidy; our MLA?
The URRC Chair noted yes; but the URRC can help by feeding back your concerns in its decision to the Minister. QEC stated now is a great time to ask URRC to report on people's concerns about the subsidy. If URRC reports on it, then there is a greater chance of subsidies getting a higher priority. The URRC Chair noted subsidy will still be a decision of the GN.

One participant questioned what happened to the same rate concept that was discussed a few years ago? The URRC Chair noted that in the 2004/2005 proceeding, it was discussed and the Minister and Executive Council decided on community based rates.

QEC commented that the recommendation at that time was to move directly in one step to a uniform rate. Now we are proposing that we move in that direction slowly, slower for fairness and slower so that rate volatility is reduced. It will take 4 to 6 GRA processes to get there.

The participant commented that he ran a small business. Rates are high now, so what will happen when the new plant is built? In response QEC stated if the plant is built and community based rates are used, the rates will rise significantly. With Nunavut wide rates, it will go down by 4% now, and the cost of the new plant will be shared across Nunavut. Nunavut wide rates appear to make the most sense for the people and the businesses.

An Elder of the Community questioned why is the increase so high? Is it the higher cost of operating and maintaining an older plant? However, he indicated he agreed with Nunavut wide rates. Community based rates are not fair for the people of Nunavut. QEC commented that the Corporation has 17 power plants near the end of their life. Operating costs are higher, and we have had no new plants since separation. QEC is now doing three plant renewal projects plus Iqaluit. Electricity is an essential service, so the rate should be the same for all.

Rankin Inlet and Cambridge Bay:

There was no community participation at the consultation meetings held in Rankin Inlet and Cambridge Bay.

5.0 COST OF SERVICE STUDIES

5.1 GENERAL

The primary purpose of a COS study is to develop a method to fairly allocate the approved revenue requirement among the different customer classes within the communities served by the utility. While there are many potential allocation methods, the core objective is to allocate costs to the customer classes consistent with principles of cost causation based on customer characteristics such as energy consumption and peak demand.

A COS study is commonly used as an analytical tool in the ratemaking process. A COS study can provide useful information such as unit costs to serve different customers (such as $/kWh, $/customer per month) and revenue to cost coverage ratios. However, any COS study involves estimation and a degree of professional judgement and therefore the results cannot be considered exact. Further, the appropriate allocation methods for a COS study will change over time as the utility's operating environment and cost drivers change.

5.2 COST OF SERVICE APPROACHES

In its 2010/11 GRA Phase I Report 2011-01, the URRC directed QEC to file the following approaches for consideration as part of its Phase II application:

- Cost of service study and rate design based on the cost of providing service by individual community;
- Cost of service study and rate design based on capital zones involving the averaging of capital related costs by region or zone. QEC should provide the rationale for grouping of communities within a zone; and
- Cost of service study and rate design based on Nunavut wide rates.

The URRC directed that the Phase II evidence should consider the pros and cons of each of the approaches and identify QEC's recommended approach, including reasons. The URRC directed that in conjunction with rate design proposals, QEC should consider the design of the subsidy program and the impacts on customers, by customer class and community. The response to this direction was to be filed within 150 days from the date of the 2010/11 GRA Phase I Report.

In response to this direction QEC filed three sets of COS studies as follows:

Community based COS study: This involves developing a community specific revenue requirement for every community. There is no sharing or averaging of plant specific costs between communities.

Capital zone based COS study: This involves averaging of capital related costs across all the communities of Nunavut, while maintaining a community based approach to non-capital operating and maintenance costs.

Nunavut wide COS study: This involves consolidating all capital and operating costs (whether they are community-based costs, regional costs or head office costs) into a single corporate revenue requirement. For this scenario, the Corporation completed a single Nunavut wide COS study for the consolidated revenue requirement.

QEC provided its evaluation of the pros and cons of each COS Study approach based on specific criteria as follows:

Cost Causation

The community based approach tracks plant-based costs at the individual community level, which allows detailed review of these cost drivers for each individual community. However, this method also requires a method for assigning head office and regional office costs to individual communities which can ultimately form a substantial portion of each community's cost structure.

The capital zone approach tracks plant-based operations and maintenance costs at the individual community level but aggregates capital based costs across Nunavut. This method still requires assigning head office and regional office operations and maintenance expenses to each community.

The Nunavut wide approach consolidates operations and maintenance costs and capital costs at the Nunavut wide level. Therefore, this method does not allow for review of different cost drivers by community. Cost drivers between rate classes are still analyzed.

Cost Stability Over Time

The community based approach is very sensitive to changes in a community's cost structure or load forecast. For example, replacement of a community's generation facility can dramatically increase the community's revenue requirement, leading to the need for material rate increases.

The capital zone approach levelizes capital costs across all communities and therefore improves cost stability over time relative to community based rates. However, sudden and unexpected changes in operations and maintenance expenses or loads in a community could still drive the need for material rate increases, particularly to the extent such changes influence the assignment of head office and regional office operations and maintenance expenses.

The Nunavut wide approach consolidates operations and maintenance costs and capital costs at the Nunavut wide level. Therefore, this method provides the highest degree of cost stability over time of the three COS study scenarios.

Consistency with Nunavut Government Policy

The community based approach results in much higher rates in isolated small communities than in larger and economically stronger ones. As such, it is not consistent with the Inuit value of helping each other, the Tamapta Action Plan objective of ensuring Nunavummiut basic needs are met, and the Government's vision of a better standard of living for those most in need.

The capital zone based approach can still result in highly unequal rates between communities as a result of sudden changes in operations and maintenance expenses or loads in a community. As such, it is not sufficiently reflective of the Government's policy objectives and Inuit societal values.

The Nunavut wide approach is better aligned with the Government's policy objectives and Inuit societal values. In particular, it better reflects the role of electricity as a basic need for customers in Nunavut, which is consistent with the Inuit value of helping each other, the Tamapta Action Plan objective of ensuring Nunavummiut basic needs are met, and the Government's vision of a better standard of living for those most in need.

Consistency with Other Utility Practices

QEC is not aware of any other regulated Crown owned utility in Canada that calculates community specific COS studies for each community. QEC is also not aware of any utility in Canada that levelizes capital costs across all communities while charging a portion of the rate for operations and maintenance expense at a community specific level in a manner consistent with the capital zone approach. Most regulated Crown utilities in Canada have some form of jurisdiction wide approach to rate-setting, at least for a portion of each customer's consumption in a manner consistent with the Nunavut wide approach.

Administrative Efficiency

The community based approach requires substantial tracking of costs by individual community. The approach also requires a method for assigning each community a share of common head office and regional office costs. Rate setting based on separate rates for each community and customer class would result in approximately 125 different rate schedules.

The capital zone approach would also require tracking of operating and maintenance costs by community and would result in approximately 125 different rate schedules.

Once the transition to Nunavut wide rates is fully implemented, the number of rate schedules will reduce to 3. QEC estimates that this process to full implementation, will take 9-10 years.

The Nunavut wide approach consolidates operations and maintenance costs and capital costs at the Nunavut wide level. This approach also does not require a method for assigning head office and regional office costs to each individual community. Therefore, in QEC's view this method is the most administratively efficient of the three COS study scenarios.

Based on the foregoing considerations, QEC states the Corporation's preferred approach is the Nunavut wide rate approach using, the Nunavut wide COS study. QEC indicates its rate design proposals are based on the results of the Nunavut wide COS study results.

URRC Findings:

The URRC's Rate Setting Guidelines provide that:

- Rates for service provided by a utility shall not be unjustly discriminatory or unduly preferential. The Review Council should base its analysis of applications on this principle and report to Government accordingly;
- Rates for utility service should be designed to encourage the wise use of energy and the Review Council should report to Government in accordance with this principle.

A principal factor that is indicative of undue preference or unjust discrimination is the cost of providing service. Unit cost differences between communities can arise from differences in vintage of plant, size of the load, customer density of the different communities, and the distance between communities and their regional centers. Although newer vintages of plants contribute to higher costs in early years under the rate base/rate of return method of regulation, over time, cost differences caused by vintage tend to level out. The URRC considers, elimination of temporary cost differences between communities, caused by vintage differences, through the averaging of costs under the Nunavut wide COS approach would not result in undue discrimination between communities.

However, largely due to economies of scale the unit cost of providing service is generally lower in larger communities compared with smaller ones, all else being equal. This is a permanent feature of cost differences between communities.

In addition to cost differences, the cost causation factors that contribute to new plant additions are important considerations in determining whether the appropriate price signals could be provided through Nunavut wide rates as compared with community based rates. In the QEC service area, the nature of the source of generation supply is diesel in all communities and the load characteristics of customer classes are approximately the same in all communities. For example in URRC-QEC 10c), QEC states the variation of community-specific customer class load factors and coincidence factors for isolated diesel systems used by other northern utilities in Canada is relatively small. Accordingly, the load drivers and planning parameters for new plant additions would be similar across the QEC service area.

In the URRC's view, a community specific COS approach best reflects cost of providing service within each community. However, given the use of diesel generation across all communities and given the similarity of load drivers contributing to new plant additions, a Nunavut wide COS approach is also an acceptable one which is consistent with the principle of cost causation and would enable the design of rates to encourage the wise use of energy.

The URRC notes QEC's submission that a Nunavut wide COS approach provides a high degree of cost stability over time. This is a desirable attribute given the small size of certain communities and the rate impact that new plant additions would cause under the community based COS approach. The URRC also notes QEC's submission that the Nunavut wide COS approach is consistent with GN policy as well as the practices of other Crown owned utilities in Canada and facilitates administrative efficiency. For all of these reasons the URRC recommends acceptance of QEC's proposal to adopt a Nunavut wide COS approach for the purpose of establishing rates.

5.3 COST OF SERVICE METHODOLOGY

5.3.1 Functionalization of Costs

The first step in a cost of service study is the functionalization of the Corporation’s plant and expenses. Functionalization refers to the separation of capital assets and operating expenses into

groups according to the specific function they perform. The Corporation has categorized its capital assets and expenses according to the following functions:

- Generation;
- Distribution; and
- General.

Functionalization of gross plant and accumulated amortization was carried out according to the Federal Energy Regulatory Commission (FERC) codes. Plant related expenses such as amortization expenses were functionalized on the same basis as the corresponding plant. Contributions by GN to capacity-increase projects were functionalized to generation while customer contributions received by QEC were functionalized to distribution. Fuel inventory amounts in working capital were functionalized 100% to generation (consistent with the functionalization of fuel expense). Other working capital amounts were functionalized to the general category.

Operating expenses were functionalized to the generation, distribution or general categories, from budget codes, according to the services performed.

URRC Findings:

The URRC notes that in the case of certain cost components such as plant operator salaries and wages, estimates were used to determine the portion applicable to the generation and to distribution functions.

In its response to URRC QEC 1-3, QEC states, in order to develop the estimate of the proportion of plant operator time spent on generation and distribution related activities, the Corporation consulted with its operations staff. The estimate is not based on a review of time sheets or similar information because such data are not currently available. The Corporation states the estimate is reasonable in the circumstances and can be relied upon for ratemaking purposes.

In the URRC's view where allocations are required to determine the amounts applicable to the generation and distribution functions, supporting information should be provided to demonstrate

the allocations reflect objective analysis, as opposed to subjective estimates. The URRC directs that, for purposes of cost functionalization, all cost items requiring allocation between the generation, distribution and general functions be supported by objective analysis at the time of the next COS Study. For the purposes of this Report, the URRC accepts the QEC proposed functionalization of costs.

5.3.2 Classification of Costs

Once costs have been sorted into functions, the next step in the COS process involves the classification of plant and expenses. The classification step involves analyzing the key cost drivers that require the Corporation to incur a particular cost. For example, capital expenditures or operating expenses might be incurred in order to meet the demand in the community at any instant in time; to meet a sustained consumption of kilowatt-hours by customers throughout the year. Such costs would be considered demand related costs driven by the coincident peak demands. Other costs may be incurred to maintain the customer account and provide billing services; such costs would be considered customer related costs. Similarly, costs related to energy consumption such as fuel costs would be energy related costs.

The proposed classification of the different cost components under the demand, energy and customer categories and the rationale based on cost causation principles is detailed in Section 4.0.

URRC Findings:

Classification of Components of Distribution Plant

For purposes of classifying the following distribution plant, QEC adopted the classification percentages used by NUL-NWT limited in its 2008-2010 GRA:

Poles and Fixtures- Customer 50%, Demand 50%
Overhead Conductors/Underground Conduits- Customer 75%, Demand 25%
Line Transformers- Weighted Customer 35%, Demand 65%

The URRC notes from URRC QEC 1-6 that there are some differences between the proposed classification percentages noted above and those used by the NTPC and the Yukon Energy Corporation (YEC). While the URRC does not disagree with the approach to determining the above classification percentages based on those from other comparable utilities, QEC specific studies would be desirable in order to establish the appropriate classification percentages for QEC, in the future. Accordingly, the URRC directs QEC to include QEC specific classification studies for poles and fixtures, overhead conductors, underground conduits, and line transformers at the time of the next COS Study.

Classification of Meter Reading, Billing and Customer Accounting

QEC included plant related costs and operating and maintenance expenses (O&M) associated with meter reading, billing and customer accounting in the general function and, these costs were in turn classified to the customer, demand and energy categories on the same basis as total generation and distribution plant.

In URRC QEC 1-7, QEC was requested to provide an analysis of the impact of classifying costs associated with meter reading, billing and customer accounting to the customer category, for the Nunavut wide COS model. QEC performed the requested analysis but noted it could not isolate general plant assets associated with meter reading, billing and customer accounting including assets such as computers and software for purposes of this analysis. QEC stated the reclassification requested in URRC QEC 1-7 resulted in a 0.2% increase in domestic COS rates, 0.1% decrease in commercial COS rates, and 1.3% decrease in street lighting COS rates.

The URRC considers costs associated with meter reading, billing and customer accounting are a material component of the general category of costs and should properly be classified on the basis of customer (or weighted customer). However, rather than disturb the Nunavut wide COS Study and the rate change proposals based thereon, the URRC directs QEC to classify meter reading, billing and customer accounting to the customer category (or weighted customer category as may be appropriate) at the time of the next COS Study. Further, when this change is implemented, the remaining general category of costs should be classified on the basis of all other costs that have been classified previously.

Non Electric Revenue

QEC proposed to classify non-electric revenues on the basis of the total of all other costs (Revenue basis). Non-electric revenue includes, joint use, miscellaneous charges as well as time and materials charges. In URRC QEC 1-9, QEC was requested to provide the impact on the Nunavut wide COS study results of treating non-electric revenues as revenue offsets to the relevant expense categories included in revenue requirement.

In its response, QEC indicated the Corporation is not able to treat the non-electric revenue as requested by the URRC, because such revenues are not forecast as offsets to specific budget expenses. Therefore, in the COS study, the Corporation treated the non-electric revenue as an offset to the revenue requirement allocated to the rate classes based on their share in total revenue from rates. This, in QEC's view, is consistent with NTPC's approach to the treatment of non-electric revenues in the COS study.

In the URRC's view, to the extent the components of non-electric revenues could be paired with the corresponding costs they should be so treated for purposes of the COS Study. Any remaining non-electric revenues may then be allocated on a revenue basis. In the URRC's view this approach would better reflect cost causation for the components of non-electric revenues. Accordingly, URRC directs QEC to direct assign as revenue offsets, those components of non-electric revenues that have corresponding expenses included in revenue requirement and to allocate the remaining non-electric revenues on a revenue basis.

5.3.3 Allocation of Costs

The final phase of the COS study involves the allocation of classified costs to customer classes based on usage characteristics. For example, production fuel costs are classified as energy-related and are allocated to customer classes based on their share of total energy sales. Allocation factors are developed for coincident peak demand, non coincident peak demand, energy sales, number of customers, weighted number of customers, and revenue offset.

URRC Findings:

Load Research

QEC states, in developing estimates of customer class load factor and coincidence factors, the Corporation reviewed the data developed by other northern utilities.

QEC indicates it carried out an analysis to test the reasonableness of the customer class load factors and coincidence factors. The analysis involved the following:

1. "Using the 2010/11 load forecast by customer class approved during the Phase I GRA and the customer class load factors and customer class coincidence factors outlined in Table 5-2 of the application to calculate a coincident peak for each customer class.

2. For each community, the Corporation created an estimated community coincident peak by summing the customer class coincident peaks derived in step 1.

3. The Corporation then compared the estimated community coincident peaks calculated in step 2, with the forecast coincident peaks from the 2010/11 Phase I GRA load forecast.

For most of the communities, (16 communities out of 25), the difference between the community coincident peak estimated in step 2 and the forecast 2010/11 peak load was within plus or minus 10%.

Based on this analysis, and noting the similarity of the operating environments between QEC, NTPC and NUL-NWT, the Corporation considered that in general the load data from other Northern utilities was relevant to QEC's circumstances."

QEC states the customer class load factor and coincidence factors used in its COS study are reasonable having regard to the fact the data used by the Corporation is in the range of data used by other northern utilities in Canada that operate isolated diesel systems. QEC states it is proposing only limited directional rate rebalancing between communities and customer classes at this time. It is unlikely that adoption of somewhat different customer class load and coincidence factors would alter the proposed rates in the current application.

Having regard to QEC's explanations noted above, the URRC accepts QEC's proposed load factors and coincidence factors for purposes of this Report.

Weighting Factors for Weighted Customer Allocations

QEC proposed that customer related costs associated with line transformers, services, meters and installations on customer premises be allocated to rate classes on the basis of weighted number of customers. For this purpose, QEC proposed a weighting factor of 1 for domestic and street light customers and 3 for commercial customers. QEC states the 3 times weighting factor for commercial reflects the fact commercial customers tend to have more complicated rate and billing structures (including demand meters for example) than domestic customers. QEC indicates the 3 times weighting factor was adopted from NTPC's 1995/98 GRA COS Study.

With respect to street lighting customers QEC states the number of street lighting customers was obtained from the meter-read sheets, which are used by the QEC operation staff to identify the current customers who have meters to be read. These meter-read sheets contain customer information only for active accounts. Generally, there is one streetlight customer per community (which is the municipality) but certain communities also have private light customers.

QEC states the Corporation did not conduct a study on determining a street lighting customers weighting factor relative to residential customers. QEC states, similar to other rate classes, street lighting customers also incur billing and customer accounting expenses. Therefore, streetlights were assigned a customer weighting factor of 1 as shown in Exhibit 6 of the COS schedules.

The URRC notes the weighting factor adopted for commercial customers from NTPC dates back to the mid-nineties and may have changed with passage of time and/or following division from NTPC. The URRC also considers the weighting factor of 1 for street lights based on a count of active accounts may not necessarily reflect the appropriate weighting of street lighting and yard lighting customers, particularly, where a municipality has more than one street light. For these reasons, URRC directs QEC to conduct a study of the appropriate customer weighting factors for domestic, commercial, street and yard lighting customers at the time of the next COS Study.

Acceptance of Nunavut wide COS Study

Subject to the foregoing comments and the directions which apply to future COS Studies, the URRC recommends acceptance of the Nunavut wide COS study as proposed by QEC and as set out in Appendix A-3 of the Application.

6.0 RATE DESIGN

6.1 RATE DESIGN OBJECTIVES

QEC states, based on its review of broad rate design and policy considerations, the Corporation has adopted the following long-term rate design objectives. QEC indicates, these long-term rate design objectives reflect a balance between the different economic and policy considerations. In QEC's view some of these long-term rate design objectives can and should be achieved immediately, while others will occur over several rate adjustments.

Rates must be set to recover the approved test year revenue requirement: This objective would allow QEC to recover its approved revenue requirement.

Move toward a Nunavut wide rate structure: This objective, in QEC's view, is better aligned with GN policy objectives and Inuit societal values. QEC states, this objective is also consistent with rate design approaches in other jurisdictions and addresses other important rate design principles, such as revenue stability, ease of understanding and administration, as well as, stability and predictability in the rate design process.

Move toward 100% revenue to cost coverage ratios for each rate class: In QEC's view this objective reflects all of the primary principles of sufficient rates, fair cost division among customers and optimal use of electricity.

Phasing-in/Magnitude of rate increase or decrease: QEC states the transition to Nunavut wide rates should be achieved gradually to minimize rate impacts to customers.

Move toward eliminating Government/Non-Government customer class distinctions: QEC indicates the distinction between these rate schedules is one of social income redistribution and not of rate design. Accordingly, QEC proposes to eliminate Government/Non-Government customer class distinctions.

QEC states the Corporation's long-term rate design objectives provide the framework for developing proposed rates effective April 1, 2012. QEC notes that not all of these long-term objectives can be achieved in a single rate adjustment. Therefore, the Corporation adopted specific rate design criteria for developing proposed rates for April 1, 2012 as follows:

Rates must be set to recover the approved revenue requirement: QEC proposed rates that would recover the approved revenue requirement for the 2010/11 test year.

Move toward Nunavut wide rates: QEC's proposed rate structure is based on a Nunavut wide COS study.

Focus rate adjustments on the energy portion of the rate: QEC states it is not proposing changes to the existing customer and demand charges, which are already levelized across Nunavut.

Phasing in rate increase/decrease: In order to minimize rate impacts to customers, QEC proposed the following constraints on rate adjustments for domestic and commercial customers for the current application:

i. Where a rate increase is indicated: a maximum rate increase of 5%; and
ii. Where a rate decrease is indicated: a maximum rate decrease of 4%.

Set street lighting rates at 100% revenue-cost coverage: QEC proposed to increase or decrease street lighting rates in order to achieve 100% revenue to cost coverage in the current proceedings.

URRC Findings:

Adoption of the proposed Nunavut wide COS study, results in significant realignment of the cost of providing service in each community. This means, required rate increases in certain communities and decreases in others in order to bring revenue to cost coverage ratios to target levels. QEC proposes the rate changes needed to bring the revenue to cost coverage ratios to target levels, by community, be gradual and carried out over a number of years in the interest of gradualism. Typically the revenue to cost target ratio is 100% with a plus or minus 5% tolerance. During the community consultation meetings, QEC stated it will take 2 – 3 GRAs to get there, and that is expected to take 9 – 10 years. For the proposed rates effective April 1, 2012, QEC proposes the maximum increase for the domestic and commercial rate class in any community be limited to 5% and the maximum decrease limited to 4%.

The URRC considers as reasonable and appropriate, QEC's proposals to phase in, over a number of years, rate changes resulting from the transition to Nunavut wide COS approach. The URRC also considers the proposal to limit the maximum increase for the domestic and commercial rate classes in any community to 5% and the maximum decrease to 4%, for rates effective April 1, 2012, to be reasonable. These proposals are consistent with the principles of gradualism and rate stability. Accordingly, the URRC recommends approval of the rate change proposals as set out in Schedules 1.1.1 to 1.1.5 of the Application.

In the URRC's view, the pace at which the transition of rates to full revenue to cost coverage takes place must be balanced against rate stability considerations. There are a number of new plant additions expected in the next few years which can contribute to rate increases. The URRC notes QEC’s statement that the combined average annual rate increases for rate-rebalancing plus cost increases for major projects and normal operating expense increases could be in the range of 10-15 per cent for some communities and customer classes in future years.[URRC QEC 1-30]

The URRC also recognizes the rates applicable to the community of Iqaluit would increase as Nunavut wide rates are phased in, which means, the level of subsidy available to domestic

customers would progressively decrease, provided the subsidy program continues in its current form.

Accordingly, for the purpose of future rate rebalancing applications URRC directs QEC as follows:

- The Nunavut wide rates should be phased in having regard to rate stability considerations including impacts on subsidy levels. The maximum increase in rates in any year due to the Phase in of Nunavut wide rates should not exceed 5%.
- The phase-in changes should be applied for only at the time QEC applies for future GRAs.

The URRC notes QEC's proposal to eliminate Government/Non-Government customer class distinctions. The URRC agrees with QEC that it would be appropriate to eliminate the distinction between Government and non-Government rates as these distinctions are not cost based. Further, elimination of the Government / non-Government distinction would facilitate administrative ease. Although QEC indicated it is in favour of eliminating Government / non-Government rate distinctions, it did not put forward any specific rate change proposals in this regard. Accordingly, URRC directs QEC to bring forward a proposal for elimination of Government / non-Government distinctions at the time of the next GRA.

6.2 CONSIDERATION OF RATE STRUCTURE

QEC indicates it is not proposing changes to the existing customer and demand charges, which are already levelized across Nunavut. In URRC QEC 1-15f), QEC was requested to comment on why it is considered just and reasonable to maintain customer and demand charges at existing levels having regard to the cost of service by rate component.

The Corporation’s proposed customer and demand charges are substantially lower than the demand and customer charges calculated by the cost-of-service study. The proposed energy charge is higher than the pure cost of service calculated by the COS study. QEC states, consistent with rate design approaches commonly used in other jurisdictions, the Corporation elected to

prioritize rate changes to the energy portion of its rate structure. Future rate adjustments could consider the merits of changes to the existing customer and demand charges.

URRC Findings:

The URRC notes QEC's view that the energy portion of the rate structure is by far the most price-sensitive component of the rate. Therefore concentrating rate increases on the energy portion of the rate increases the price signal to the customer. [URRC QEC 1-15f)]

While the URRC agrees the energy piece of the rate structure dictates energy price sensitivity there are also other considerations in establishing just and reasonable rates. In this regard the URRC considers it important to provide the appropriate price signals to encourage the wise use of energy. For commercial rates which include a demand component it is just as important to provide the appropriate price signals respecting peak time use as it is to provide the energy use price signals.

The URRC also considers the structure of rates to be important in mitigating intra-class rate disparities. A low percentage recovery of fixed costs through fixed charges may result in relatively high energy use customers within the same rate class cross subsidizing low energy use customers.

For all of the above reasons, the URRC directs QEC to examine the rate structures for domestic, commercial and lighting customers at the time of the next Phase II GRA in light of the corresponding costs by rate component. The URRC recommends acceptance of the rate structures as proposed, for the purposes of these proceedings.

7.0 FUEL STABILIZATION FUND ADJUSTMENTS

The Fuel Stabilization Fund (FSF) and Fuel Stabilization Rider (FSR) were established in 2005/06 following review of the Corporation’s 2004/05 GRA. The objective of the FSF is to mitigate the risk and manage the rate volatility related to fuel price changes. The fund operates

pursuant to the procedures set out in Schedule F1 of the Minister's Instruction to QEC from February 17, 2006.

Each month, the fund is charged or credited with any fuel price variances relative to the fuel prices included in base rates as part of the Corporation's last approved test year. These amounts are deferred in the fund and accumulate until the fund reaches the threshold of plus or minus $1 million. When the threshold is reached, the Corporation applies to the responsible Minister to implement a Nunavut wide rider calculated to recover or refund the accumulated balance in the fund over a six month period. QEC proposed two changes with respect to how the fund is operated.

First, QEC proposed that interest not be charged on fund balances. In this regard QEC noted the practice of not charging interest on the rate stabilization fund balance was reviewed as part of the Corporation's October 4, 2010 Fuel Stabilization Rider (FSR) application proceeding. In its report respecting the above application, the URRC accepted QEC's proposal that interest not be charged or credited for purposes of the FSR proceeding and recommended that the Corporation addresses any change to the Ministerial Directive as set out in Schedule F1 as part of the 2010/11 GRA.

QEC submitted that, considering that (i) interest has not been charged to the fund balances from the start of the fund; (ii) that no concern has been raised during the past six years with respect to this practice; and (iii) that based on the review of the fund balance since its implementation, foregoing interest charges to the fund is a benefit to customers. The Minister's Instruction should be amended to remove the interest charges on the FSF balances.

Second, QEC proposed, the use of a single Nunavut wide weighted average fuel price and a single Nunavut wide weighted average fuel efficiency factor for calculation of the rate stabilization fund balance and FSR. QEC proposed the following format for the FSF calculations in Appendix C of the Application:

Fuel Stabilization Rider Application Format				
		Month 1	Month 2	Month 3
1	Actual/Forecast Diesel Generation (MWh)			
2	Weighted Average 2010/11 GRA Fuel efficiency (KWh/L)			
3	Litres of Fuel Required (000 Litres)			
4	Weighted Average Actual/Forecast Fuel Price ($/L)			
5	Weighted Average GRA Fuel Price ($/L)			
6	Increase /Decrease in Fuel Price ($)			
7	Additional Diesel Cost ($000)			
	Fuel Stabilization Fund Continuity ($000)			
8	Opening Deficiency/Surplus			
9	Refund/Collection Rider			
10	Additional Diesel Cost			
11	Closing Balance			

QEC states the format change will not impact the underlying calculation of fund balances but will simplify the review of the FSR applications. QEC submitted that the Corporation will deal with the recovery (credit) of any outstanding (surplus) fund balance, as well as any Government contribution against the fund balance, as part of its next FSR rider application.

URRC Findings:

Interest on Fund Balances

Schedule F-1 states interest shall be charged to or deducted from the rate stabilization fund balance based on short term interest rates. In the URRC's view, the purpose of this clause is to ensure a fair balance between customers and the utility in bearing the burden of carrying costs associated with any substantial FSF balances that may occur from time to time. In the URRC's view, the interest clause in Schedule F-1 continues to be appropriate for this purpose. However, based on administrative costs and materiality considerations the Corporation may choose to request waiver of the interest rate charge or credit to the FSF.

Accordingly the URRC directs the relevant clause in Schedule F-1 of the Minister’s Instruction to QEC from February 17, 2006, be amended as follows:

Interest shall be charged to or deducted from the rate stabilization fund balance based on short term interest rates. At the time of each FSR application QEC may request approval for waiver of the interest charge for a given period having regard to materiality of the charge and the administrative costs involved.

Nunavut wide Fuel Price and Efficiency Factors

While the proposed format for presentation of FSR applications is acceptable, the URRC considers certain additional information should be included in the filings for examination and testing of FSR applications.

First, a supporting schedule should be provided showing the calculation of the weighted average actual/forecast fuel price, using actual volumes, by community. The same actual/forecast volumes should be used in conjunction with GRA forecast fuel prices to calculate the weighted average GRA fuel price. Second, a schedule should be provided showing the actual fuel use in liters, conversion to kWh of generation using GRA approved fuel efficiencies by community, losses, sales and rider collections/refunds by community. Subject to the inclusion of the additional information noted above, the URRC directs the adoption of the format for FSR applications proposed by QEC, for future FSR applications.

8.0 TERMS AND CONDITIONS OF SERVICE

The Corporation proposed certain changes to its Terms and Conditions (T&Cs) of Service. QEC states the changes, in general, are intended to:

- Provide greater clarity and consistency;
- Make the document easier to understand by both customers and the Corporation's personnel;
- Address issues or gaps that have been identified over the past number of years; and
- Better align the Corporation's terms and conditions with industry practice for other Northern utilities in Canada.

The URRC through its information requests, examined QEC with respect to a number of clauses in the proposed T&Cs, during the proceedings. As a result of this examination QEC filed a revised set of T&Cs in its response to URRC QEC 3-36 Attachment.

The specific issues of concern to the URRC are discussed below.

8.1 DEMAND CHARGE

Clause 2.13 states:

> ".. the Demand upon which billing to a Customer is based and may be estimated or measured by an approved Demand Meter. Unless otherwise specified in the Corporation Rate Schedule, the Demand shall be the greater of the current month's demand or the maximum Demand experienced during the 12-month period ending with the current billing period for determination of Demand Charges. The Billing Demand shall not be less than 5 kW per month at the applicable rate as per schedule "C"."

QEC states for smaller commercial customers without installed demand meters, and who normally would not be expected to exceed 5 kW peak demand each month, the invoices for service are based on a 5 kW minimum monthly consumption, consistent with the approved rate schedules.

URRC Findings:

The URRC is concerned that there are commercial customers without installed demand meters. URRC's concern is QEC's expectation that smaller customers without demand meters would not exceed 5 kW billing demand; this may or may not be true. There is also a concern that the fixed minimum charge based on 5kW demand may not be an appropriate minimum charge for customers without demand meters. URRC directs QEC to address these concerns at the time of the next GRA.

8.2 CUSTOMER GENERATION

Clause 3.5 provides as follows:

> "A Customer must sign an agreement with the Corporation if the Customer wishes to use Service:
> a) In parallel operation with; or
> b) As supplementary, auxiliary or stand-by Service to any other source of Energy.
>
> Service run in parallel or as supplementary Energy must be approved by the Corporation to ensure it meets the Corporation's interconnection guidelines and any applicable regulatory requirements.
>
> Retail stand-by service to back-up customer self-generation may be provided by the Corporation where surplus capacity is available. The Utility Rates Review Council shall recommend and the Responsible Minister shall approve the rates for such service."

In its response to URRC QEC 23, QEC indicates the Corporation does not currently have interconnection guidelines for customers wishing to operate their own generation in parallel with QEC electricity service. The Corporation also does not currently have a rate proposal for such service, because, to date no customers have requested such service.

QEC states the Corporation is in the process of developing a Net Metering Policy and Independent Power Producer Policy. Interconnection Guidelines will be reviewed as part of the review of these policies. The Corporation would seek the necessary approvals from the responsible Minister following completion of the policies.

URRC Findings:

In the URRC's view Clause 3.5 of the T&Cs appears redundant in the absence of the relevant interconnection guidelines and policies on applicable regulatory requirements referred to therein. Accordingly, URRC directs QEC to add a notice to reader under Clause 3.5 to indicate the interconnection guidelines are currently under development and to provide guidance on how requests for interconnection would be dealt with in the interim, pending implementation of the guidelines.

8.3 INTEREST AND REFUND OF DEPOSITS

Clause 5.8 Revised as per URRC QEC 3-36 attachment provides as follows:

> "The Corporation will pay simple interest on the security deposit from the date the deposit is paid, at an annual rate of interest equal to the Daily Interest Savings rate in effect at the end of each month as posted by the Canadian Imperial Bank of Commerce. Such interest will be credited monthly to the Customer's security deposit account for each full month that the security deposit is held by the Corporation. Security deposits and interest will be applied to the Customer's account after 1 continuous year of good credit history with the Corporation upon receipt of a Customer's request. When the Customer is disconnected from Service, security deposits and interest will first be applied to the Customer's account to cover any balance owing, then any remaining credit will be refunded to the Customer.

When questioned in URRC QEC 35 as to why security deposits and interest will be applied to the Customer's account after one continuous year of good credit history with the Corporation **only** upon receipt of a Customer's request QEC states, the Corporation faces frequent turnover of its customers across Nunavut and does not have the necessary resources to automatically identify all customers with one continuous year of good credit history with the Corporation. However, QEC indicates it is able to check the credit history of a specific customer, at the customer's request, to determine if he/she has had one continuous year of good credit history with the Corporation.

URRC Findings:

The URRC notes other Crown owned utilities such as NTPC pay simple interest on the Security Deposits from the date the deposit is paid, at the rate specified from time to time in the Residential Tenancy Act of the Government of the Northwest Territories. Further, such interest is credited to the customer's account on the first bill following December 31 of each year or when the deposit is refunded.

The URRC considers customers should not have to request interest to be credited on their security deposit balances. Interest accrued on individual security deposits in a given year should be calculated and recorded in that same year. This will be consistent with good utility practice.

Accordingly, URRC directs QEC as follows:

- Initiate necessary changes to the accounting system so that interest will be credited automatically to individual security deposit accounts without the customer having to request same.
- Amend clause 5.8 of the T&Cs accordingly.

8.4 DEPOSITS FOR INSTALLATIONS AND MAINTENANCE SERVICE

Clauses 7.2 and 7.5 refer to deposits being required for installations and maintenance services. However, they do not explain how the deposit amounts would be determined. In URRC QEC 36 the Corporation was requested to provide further clarification on how the deposit amounts are to be determined.

In response QEC provided the revised versions of clauses 7.1, 7.2 and 7.5 which make specific reference to contracts for service, for the determination of deposit amounts.

URRC Findings:

The URRC accepts the revised versions of clauses 7.1, 7.2 and 7.5 as set out in URRC QEC 3-36 Attachment.

8.5 METER READINGS AND ESTIMATES

Clause 12.1 provides in part as follows:

> "In the case of metered Service, the invoices for Service provided to the Customer shall be based upon actual meter readings. In circumstances where the Corporation is not able to obtain meter readings for any reason including, without limitation, dogs, locked doors, weather conditions, vandalized equipment, or equipment failure, invoices for Service shall be based upon meter readings estimated by the Corporation. These estimates will be adjusted if and when actual meter readings are obtained."

QEC indicates that the Corporation does not have an established policy on the maximum length of time for meters to remain unread. Considering the northern climate conditions that the

Corporation operates under, some meters may not be read on a monthly basis for many reasons (e.g. the site is inaccessible due to weather, customers' dogs, locked doors, etc). In situations where meters remain unread for greater than two months the Corporation addresses these situations on a case-by-case basis.

QEC was not able to provide any statistics respecting the frequency distribution of meters that remained unread for over two months. However, QEC indicates that the Corporation prepares regular inserts into the customer bills explaining to the customers the importance of resolving the problems with meter access. The Corporation indicates it works with customers directly educating them on their responsibilities for providing meter read access for the Corporation's employees.

QEC indicates that outside the regular monthly site visits, QEC staff makes special effort by doing the following:

- Contacting landlords of utility/mechanical rooms that contain meters for multi units to obtain new keys for changed locks.
- In unique circumstances QEC makes special provisions by upgrading the standard meter with digital meters that are easier to read and can be read from a further distance.
- Office staff will contact customers to emphasize the importance of gaining access to perform actual meter reads and work with them to help improve the situation.

URRC Findings:

The URRC considers the absence of a policy on how long meters can remain unread is not consistent with good utility practice. The URRC is also concerned that the Corporation does not maintain any statistics on unread meters. Although QEC indicates it takes steps to follow up on unread meters, the absence of statistics would appear to make this process a hit and miss approach.

Accordingly, URRC directs QEC as follows:

- Within 30 days of release of this Report to develop a policy on how long meters can remain unread and implement any procedural changes necessary to comply with this policy.
- Develop and maintain the necessary statistics to record and report unread meters at any given point in time so that timely action may be initiated.

In addition, the URRC notes from its Final Report on the 2004/05 General Rate Application dated February 18, 2005, page 81, paragraph 1, QEC's statement during examination, that it was considering making available a budget plan for customers who wanted to levelize their payments. To this end, the URRC believes such a plan, if made available to customers might assist QEC and its customers for whom access to the electricity meters cannot be guaranteed year round. This might be especially valuable in mitigating the effects on customers of significant rate changes such as the recent 18.88% increase to base rates, smoothing changes resulting from the move from community based rates towards Nunavut wide rates, and reducing customer concerns respecting bill volatility from season to season. Such a program would likely enhance QEC's cash flows throughout the year and at the same time resolve many customer concerns about bill volatility. Accordingly, the URRC directs QEC to assess the benefits and costs of implementing a levelized monthly customer payment plan and to bring it forward at the time of QEC's next GRA. The URRC directs QEC to include a review of the appropriate frequency of meter reading true-ups for customers so that it achieves the maximum benefit for both QEC and its customers.

8.6 SCHEDULE C-FEES AND SERVICE CHARGE SUMMARY

The proposed fees and service charge summary is set out in Schedule C of the T&Cs.
QEC indicates the Corporation's service connection charges are the same as NTPC's and were approved by the Northwest Territories Public Utilities Board (NWTPUB) prior to the division of the Territories. QEC indicates it has not applied to change the service connection charges. QEC

states in the event the Corporation applies to change its service connection charges in the future, it will provide information related to the cost basis for the proposed changes.

URRC Findings:

The URRC considers while the fees and service charges of comparable utilities are relevant considerations it is best to establish QEC's fees and service charges using QEC's cost structure as the primary basis. This is important irrespective of whether QEC is requesting a change in its fees and service charges or not. Accordingly, URRC directs QEC to provide the cost basis for QEC's proposed fees and service charges included in Schedule C based on QEC's unique circumstances, at the time of the next GRA.

9.0 RESPONSE TO URRC DIRECTIONS

9.1 PHASE II RELATED DIRECTIONS ARISING FROM URRC REPORT 2011-01

Directive #2 on Demand Side Management (DSM) and other conservation programs states:

> "The URRC directs QEC to identify and develop cost effective DSM and other conservation programs with a view to offsetting some of the projected demand growth in the next 5 to 10 years."

With respect to this directive the letter to the URRC by the Minister responsible for QEC, dated May 26, 2011 states in part:

> "QEC will coordinate with the Energy Secretariat on cost-effective DSM and other conservation programs to ensure there is no duplication of services and interests of the rate payers are duly considered."

URRC Findings:

The URRC encourages QEC to bring forward any DSM and conservation initiative that have rates and rate design implications for review and approval by the responsible Minister on a timely basis as and when they are ready for implementation without necessarily waiting for the next GRA. The URRC directs that updates with respect to DSM and conservation initiatives should be provided at the time of the next GRA.

Directive #3 on helping customers better manage their electricity consumption, states:

> "In addition, the URRC directs QEC to give consideration to helping customers better manage their electricity consumption. This may include customer education, as well as rate design changes promoting wise use of energy. Further, a reassessment of the design of the subsidy programs would be appropriate to make customers more aware and accountable for their consumption decisions."

With respect to this directive the letter to the URRC by the Minister responsible for QEC, dated May 26, 2011 states in part:

> "..energy conservation programs have been assigned to the Energy Secretariat and all subsidy programs are delivered by the GN. However QEC will make every effort within its mandate in providing assistance and input into both initiatives."

URRC Findings:

The URRC has commented on conservation programs and subsidy programs under Directives 2 and 16, in this Section.

Directive #6 on use of single weighted average fuel price and fuel efficiency states:

> "With respect to QEC's suggestion that use of a single weighted average fuel price (both forecast and actual) and a single weighted average fuel efficiency should improve the administrative burden of maintaining the Fuel Rate Stabilization Fund and simplify the review process, the URRC considers this matter is best addressed in the Phase II proceeding. Accordingly, QEC is directed to address this matter in its Phase II filing."

URRC Findings:

The above directive is dealt with in Section 7 of this Report. The URRC considers the directive has been complied with.

Directive #14 on FSR consolidation into base rates states:

> QEC has not specifically applied for the roll in of the FSR in the current application and the URRC considers the consolidation of the 4.68¢ kWh FSR as part of the base rates is a matter best addressed at the Phase II proceedings dealing with rate structure, at which time customers ought to be explicitly notified as to QEC's proposal. URRC directs QEC to bring forward its application to consolidate the FSR into base rates at that time.

In its response to this directive QEC stated:

> Since the fuel prices included in base rates as at April 1, 2011 were equal to the most current actual fuel prices, there was no longer a need to implement a FSR rider (since the variance between fuel prices included in base rates and actual fuel prices was zero and the balance in the FSR at April 1, 2011 was below the trigger level). Therefore, concurrent with the 18.88% increase to the energy portion of base rates, QEC, terminated the fuel rider of 4.68¢/kWh effective April 1, 2011.

URRC Findings:

The URRC accepts the above explanation and considers the directive has been complied with.

Directive #16 on alternative approaches to cost of service studies and rate design states:

> "Accordingly, QEC is directed to file the following approaches for consideration as part of its Phase II application:
>
> - Cost of service study and rate design based on the cost of providing service by individual community;
> - Cost of service study and rate design based on capital zones involving the averaging of capital related costs by region or zone. QEC should provide the rationale for grouping of communities within a zone; and
> - Cost of service study and rate design based on Territory-wide rates.
>
> The Phase II evidence should consider the pros and cons of each of the approaches and identify QEC's recommended approach, including reasons. In conjunction with rate design proposals, QEC should consider the design of the subsidy program and the impacts on customers, by customer class and community. The response to this direction should be filed within 150 days from the date of this Report."

In response to the above directive QEC stated:

> "The Corporation has provided the three cost of service study scenarios as requested in Chapter six of the Application. Chapter six also includes a discussion of the advantages and disadvantages of each approach and recommends the territory wide COS study as the preferred method. The Corporation's approach to rate design is described in Chapter seven. In consideration of the impact of rate adjustments on customers, the Corporation applied a 5% rate cap on rate increases in the current application.
>
> With respect to the subsidy program, the Corporation notes that the subsidy is a program of the Territorial government. As such, the Corporation does not set the terms of the subsidy program. However, the Corporation notes that Cabinet has directed that a review of the subsidy program be undertaken. The Corporation will provide recommendations to

the Territorial government with respect to revisions to the subsidy program that may be undertaken."

URRC Findings:

With respect to the first part of the directive, respecting alternative cost of service studies and rate design approaches, the URRC considers that portion of Directive 16, has been complied with.

With regard to the second part, on the rate design aspect of the subsidy program, the URRC directs that any changes with respect to the subsidy program be addressed at the time of the next GRA.

9.2 PHASE II RELATED DIRECTIONS ARISING FROM THE URRC'S 2004/05 GRA REPORT

Directive on service connection fees from page 83 states:

> "The URRC directs QEC to address the cost basis for service connection fees at the time of the next GRA."

URRC Findings:

QEC has failed to comply with this directive. This matter is dealt with in Section 8.6 of this report.

10.0 SUMMARY OF URRC DIRECTIONS

1. The URRC directs that, for purposes of cost functionalization, all cost items requiring allocation between the generation, distribution and general functions be supported by objective analysis at the time of the next COS Study.

2. The URRC directs QEC to include QEC specific classification studies for poles and fixtures, overhead conductors/underground conduits and line transformers at the time of the next COS Study.

3. The URRC directs QEC to classify meter reading, billing and customer accounting to the customer category (or weighted customer category as may be appropriate) at the time of the next COS Study. Further, when this change is implemented, the remaining general category of costs should be classified on the basis of all other costs that have been classified previously.

4. URRC directs QEC to direct assign as revenue offsets, those components of non-electric revenues that have corresponding expenses included in revenue requirement and to allocate the remaining non-electric revenues on a revenue basis.

5. The URRC directs QEC to conduct a study of the appropriate customer weighting factors for domestic, commercial, street and yard lighting customers at the time of the next COS Study.

6. Accordingly, for the purpose of future rate rebalancing applications URRC directs QEC as follows:

- The Nunavut wide rates should be phased in having regard to rate stability considerations including impacts on subsidy levels. The maximum increase in rates in any year due to the Phase in of Nunavut wide rates should not exceed 5%.
- The phase-in changes should be applied for only at the time QEC applies for future GRAs.

7. The URRC directs QEC to bring forward a proposal for elimination of Government non Government distinctions at the time of the next GRA.

8. The URRC directs QEC to examine the rate structures for domestic, commercial and lighting customers at the time of the next Phase II GRA in light of the corresponding costs by rate component.

9. The URRC directs the relevant clause in Schedule F-1 of the Minister's Instruction to QEC from February 17, 2006, be amended as follows:

> *Interest shall be charged to or deducted from the rate stabilization fund balance based on short term interest rates. At the time of each FSR application QEC may request approval for waiver of the interest charge for a given period having regard to materiality of the charge and the administrative costs involved.*

10. Subject to the inclusion of the additional information noted above, the URRC directs the adoption of the format for FSR applications proposed by QEC, for future FSR applications.

11. The URRC is concerned that there are commercial customers without installed demand meters. The concern is the QEC expectation that smaller customers without demand meters would not exceed 5 kW billing demand; this may or may not be true. There is also a concern that the fixed minimum charge based on 5kW demand may not be an appropriate minimum charge for customers without demand meters. URRC directs QEC to address these concerns at the time of the next GRA.

12. The URRC directs QEC to add a notice to reader under Clause 3.5 to indicate the interconnection guidelines are currently under development and to provide guidance on how requests for interconnection would be dealt with in the interim, pending implementation of the guidelines.

13. The URRC directs QEC as follows:

- Initiate necessary changes to the accounting system so that interest will be credited automatically to individual security deposit accounts without the customer having to request same.

- Amend clause 5.8 of the T&Cs accordingly.

14. The URRC directs QEC as follows:
    - Within 30 days of release of this Report to develop a policy on how long meters can remain unread and implement any procedural changes necessary to comply with this policy.
    - Develop and maintain the necessary statistics to record and report unread meters at any given point in time so that timely action may be initiated.

15. The URRC directs QEC to assess the benefits and costs of implementing a levelized monthly customer payment plan and to bring it forward at the time of QEC's next GRA. The URRC directs QEC to include a review of the appropriate frequency of meter reading true-ups for customers so that it achieves the maximum benefit for both QEC and its customers.

16. The URRC directs QEC to provide the cost basis for QEC's proposed fees and service charges included in Schedule C based on QEC's unique circumstances, at the time of the next GRA.

17. The URRC encourages QEC to bring forward any DSM and conservation initiative that have rates and rate design implications for review and approval by the responsible Minister on a timely basis as and when they are ready for implementation without necessarily waiting for the next GRA. The URRC directs that updates with respect to DSM and conservation initiatives should be provided at the time of the next GRA.

18. The URRC directs that any changes with respect to the subsidy program be addressed at the time of the next GRA.

11.0 URRC RECOMMENDATIONS TO THE RESPONSIBLE MINISTER

1. The URRC recommends acceptance of QEC's proposal to adopt a Nunavut wide COS approach for the purpose of establishing rates.

2. The URRC recommends acceptance of the Nunavut wide COS study as proposed by QEC and as set out in Appendix A-3 of the Application.

3. The URRC recommends approval of QEC's rate change proposals as set out in Schedules 1.1.1 to 1.1.5 of the Application, effective April 1, 2012.

4. The URRC recommends adoption of the changes to the operation of the rate stabilization fund described in Directions #9 and #10 of Section 10.0 of this Report.

5. The URRC recommends approval of the Terms and Conditions of service as set out in URRC QEC 3-36 Attachment, subject to the changes referred to under Directions #12 and #13 of Section 10.0 of this Report.

6. Nothing in this Report shall prejudice the URRC in its consideration of any other matters respecting QEC.

ON BEHALF OF THE

UTILITY RATES REVIEW COUNCIL OF NUNAVUT

DATED: January 27, 2012

Raymond Mercer

Chair